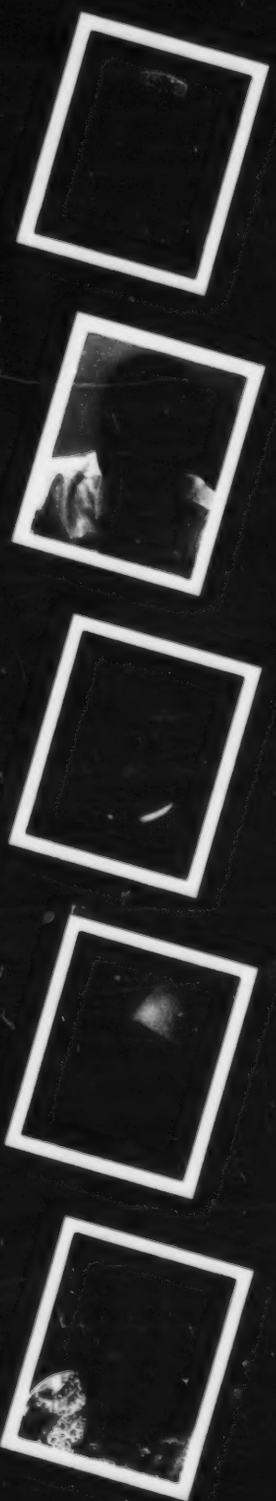
MARITIME ELECTRIC COMPANY, LIMITED

1988 ANNUAL REPORT



FINANCIAL HIGHLIGHTS

	1988	1987
Operating revenue	$ 59,866,283	$ 61,111,248
Operating expenses	41,518,144	43,209,523
Net earnings	5,274,769	5,121,252
Earnings per common share	1.42	1.34
Dividends declared per common share	0.80	0.77
Capital expenditures (net)	11,600,127	11,237,712
Gross fixed assets	$136,023,249	$125,594,574
Sales (kWh)	618,700,000	579,800,000
Number of customers	48,600	47,500
Number of common shareholders	1,742	1,470

Common Share Quarterly Statistics

1988	First	Second	Third	Fourth
Earnings per share	$ 0.53	0.29	0.56	0.04
Dividends declared per share	$ 0.20	0.20	0.20	0.20
Share price[1] — high	$ 12	13	12 5/8	13 1/4
— low	$11 1/2	11 5/8	12 1/8	12
Shares traded[2] (000's)	38.5	133.6	25.8	56.6

1987	First	Second	Third	Fourth
Earnings per share	$ 0.47	0.29	0.40	0.18
Dividends declared per share	$ 0.19	0.19	0.19	0.20
Share price[1] — high	$14 1/2	14 1/2	14 1/4	12 1/8
— low	$13 1/8	13 1/4	12 1/4	10 1/4
Shares traded[2] (000's)	92.7	52.2	52.6	78.7

[1] Prices quoted on the Toronto Stock Exchange.

[2] Combined volume of shares traded on the Toronto and Montreal Stock Exhanges.

Overview 1988

During the year Maritime Electric Company, Limited completed seventy years of operations on Prince Edward Island. It was another successful year for our Company, our customers and our shareholders. The net assets of the Company exceeded the $100 million level. Our customers enjoyed further reductions in electricity prices. Dividends declared and paid increased for the 13th successive year.

Sales of electricity by the Company continued the upward trend which was re-established in 1983 following the 1981-82 recession. In 1988 we saw a 6.7 percent increase in sales over 1987. This increase in sales reflects a greater level of activity in the Company's commercial customers, a growth in the number of residential customers and an increase in the average use by this class of customer. This, coupled with the control of operating expenses, allowed the Company to earn its allowed rate of return while returning to our customers almost $900,000 in revenue surplus to revenue requirement.

The benefits of increased sales and reduced costs have been shared between the Company's customers and shareholders. Customers benefitted in that the average cost of electricity was 8.2 percent lower than in 1987. Net earnings for the year were $5.3 million as compared to $5.1 million in 1987. Earnings per common share increased from $1.34 in 1987 to $1.42 in 1988, and in keeping with the Company's policy of paying out approximately half of common share earnings, four common dividends of 20 cents were declared during the year.

Operations

To supply our customers' energy needs the Company generated or purchased 696.2 million kilowatt-hours of electricity, an increase of 6.7 percent over 1987. Over 32 percent of the Island's requirements, amounting to 223.4 million kWh, were obtained from Company owned sources located on the Island and in New Brunswick; while 295.2 million kWh of interruptible and 177.6 million kWh of contract energy were purchased directly from NB Power.

Sources and Costs of Electric Energy

	Net kWh (Millions)	Unit costs ¢/kWh
Charlottetown Steam Plant	83.8	4.1
Dalhousie II (Coal-Oil Plant)	132.8	3.1
Borden Gas Turbine Plant	6.8	9.2
Contract Energy	177.6	3.3
Interruptible	295.2	3.1

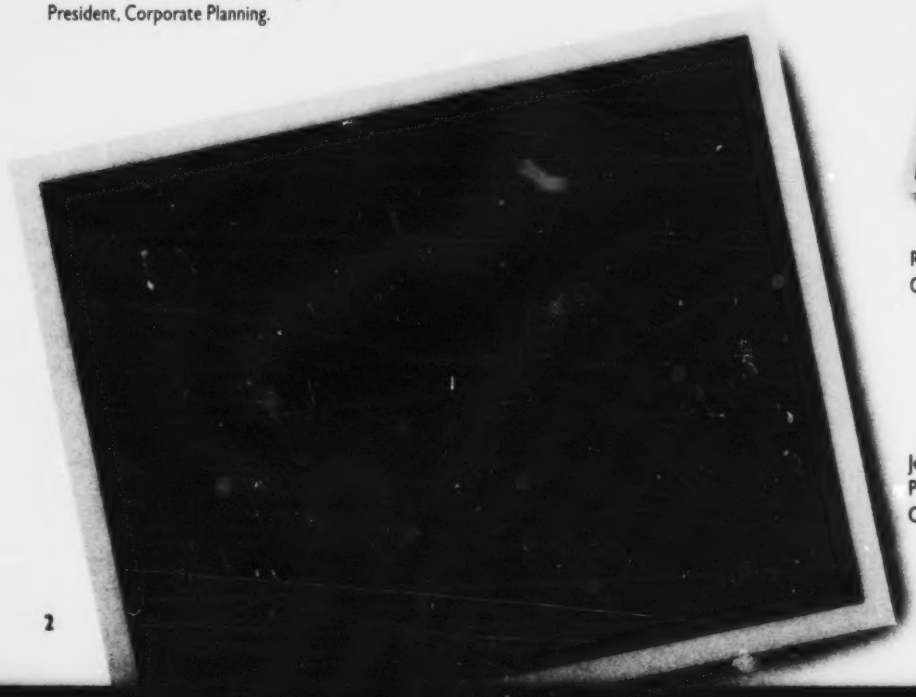
Maritime Electric's 10 percent ownership interest in the 200,000 kilowatt coal-oil fired No. 2 Unit at Dalhousie, New Brunswick was purchased in 1981-82 to help stabilize the Company's energy costs and reduce its dependence on oil. The unit continued to perform efficiently in 1988, its equivalent average fuel cost being 3.1 cents per kilowatt-hour.

Every three years the Company inspects the submarine cable portion of the interconnection between our system and NB Power. This inspection was made in 1988. The cable facilities were determined to be in excellent condition. There is, however, a requirement to do some remedial work on the burial of the cable at the New Brunswick side of the crossing.

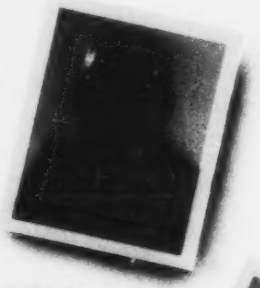
A major item of maintenance expense on repair of the #2 Gas Turbine in 1988 was a complete rebuild of the exhaust stack and silencer.

Maritime Electric is concerned about our environment and has responded to problems with stack emissions at our Charlottetown plant. This issue came to the forefront early in the year with the increased operation of the plant. In October, the results of a detailed study of the situation were released to the public. In the interim we maintained a dialogue with the media and residents near the plant.

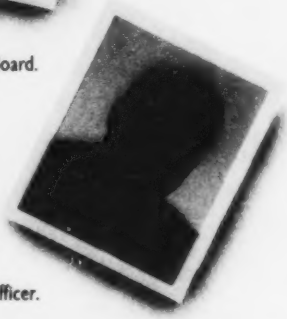
To neutralize the acidity in the stack emissions we are installing $460,000 worth of equipment that will inject magnesium hydroxide into the flue gas as it leaves the boilers.



Maritime Electric's newly structured Executive team poses in the theatre of Charlottetown's Confederation Centre for the Arts, a regular focus of the Company's cultural support programs. L-R: James A. Lea, Vice-President, Customer Service and Energy Management; Paul H. Newcombe, Vice-President, Engineering and Operations; Douglas K. McKenney, Vice-President, Finance and Administration; John H. Reynolds, President and Chief Executive Officer; Michael A. Pavey, Vice-President, Corporate Planning.



R.W. Smith, Chairman of the Board.



John H. Reynolds, President and Chief Executive Officer.

This process should significantly reduce the particulates deposited within the immediate vicinity of the Plant. We are investigating other measures and monitoring the situation closely to ensure that the emission of the particulates is dispersed in an environmentally safe manner. As responsible corporate citizens we are concerned about the environment in which we live and operate.

Staff

The Company and our employees' union, the International Brotherhood of Electrical Workers, signed a new, two-year agreement in October. This collective agreement is effective 1 July 1988 to 30 June 1990.

The Company initiated a salary administration program for our salaried employees. This program enhances our ability to reward good performance based on a formal evaluation, using agreed, measurable criteria. Another benefit of this plan is its close relation to the factors of job description and evaluation listed in the Canadian Human Rights Act and Equal Pay Guidelines. We now have an appropriate structure in place to respond to any changes in Pay Equity legislation.

The number of employees grew from 202 to 221 in 1988. In 1987, management, while exploring the possible purchase of the Electric Power System of the Town of Summerside, had imposed a Company wide hiring freeze to allow greater flexibility in integrating staff from the two organizations. The hiring freeze was lifted in late 1987 after the Town declined to take up the Company's offer to purchase. Consequently, 1988 was a "catch up" year with respect to staffing. Many of our new employees were hired to work in the Charlottetown Plant, a reflection of its increasing use as load grows and the plant becomes more economical in a regime of low oil prices.

Another area where we welcomed several new employees was our Line Department. In anticipation of future needs arising from retirement, we have started several new apprentice linemen on the four-year path to Journeyman Lineman status.

Once again the dedication of our employees has helped us attain our goals and the Directors extend their appreciation for the tremendous contribution of our employees. In 1988 we initiated new programs seeking additional input from our employees; these will continue into the future. We recognize the vital role our employees can play in helping the Company meet the changing needs and the challenges facing us in the future. In response to this, we are committed to enhancing two-way communications with all our employees.

Planning

In fulfilling our responsibility to plan for the future needs of our customers, the Company is constantly examining all options for generation additions and transmission development, with the goal of identifying the least cost alternatives over the long term. In July 1987 and February 1988, Maritime Electric appeared before the Public Utilities Commission in our first, formal Advance Plan Hearing.

The Company indicated that, while there may be some potential for additional Island generating capacity, the most cost effective method of meeting the bulk of the Island's growing energy needs is through participation in new, large generating units on the mainland. Since the opportunity to participate in new mainland generation would not be available until the early 1990's, we proposed that intermediate firm capacity and energy purchases be used to meet growing Island requirements in the interim.

During these hearings the Commission's expert witness, Dr. George C. Baker, confirmed the appropriateness of the Company's planning approach when he reported, "The approach used by the Utility is in my opinion perfectly solid and I cannot suggest any improvements in the approach taken. The review procedure instituted by the Commission is in my opinion a constructive part of the planning process . . . ." Acceptance of the Company's

Always prepared as a Meter Reader, Paul Gauthier of Charlottetown is understandably very active in the Island Scouting movement.

planning methods and proposals was reflected in the Commission's decision in March 1988. The Commission has advised that the Advance Plan review take place on a triennial basis.

Following through with our planning proposals, Maritime Electric, in conjunction with NB Power, Hydro Quebec and the governments of Prince Edward Island, New Brunswick and Quebec, negotiated a purchase

of up to 50 MW of capacity and 2975 GWh of firm energy from NB Power over a six-year period beginning November 1, 1988. The Public Utilities Commission approved this purchase on November 30, 1988.

This contract gives the Company access to firm capacity and firm energy — one independent of the other, at prices unrelated to oil prices. It provides an effective hedge against rising oil prices and reduced availability of interruptible energy. At the same time, the Company retains the ability to take advantage of lower oil prices and interruptible energy when the opportunity arises.

Our examination of the longer term generation options also includes consideration of extending the useful life of the Charlottetown Steam Plant. Electric utilities are increasingly recognizing the cost effectiveness of refurbishing existing facilities rather than building replacement plants.

We are continuing our demand-side management strategy through our "Beat the Peak" campaign. This year we repeated our newspaper and radio advertising asking all energy consumers to reduce their consumption of electricity between the hours of 4:00 p.m. and 7:00 p.m. Our customers responded enthusiastically again this year, enabling us to meet our objectives and improve our load factor.

As part of our strategic planning efforts we are continuing our examination of other options related to demand-side management.

Federal Regulation

The Company remains aware that our unique situation at the end of the Canadian energy chain demands constant monitoring. We continue to review developments in energy legislation and to represent Island interests with respect to electricity costs and security of supply.

In response to possible changes in federal legislation which could allow Canadian utilities exporting electricity to sell electricity to the United States at lower prices than to Canadian utilities, we asked our customers to show their concern by contacting their Members of Parliament. An unprecedented number of our customers responded. The collective voice of our customers was echoed by the provincial government and heard by the federal government. Our concerns were properly addressed in the changes to the national export policy announced by the Honorable Marcel Masse.

Organization Structure

In response to the continuing growth of the Company's utility operations and the increasing demand for senior management time the Company's executive structure was reorganized effective December 1, 1988.

Paul H. Newcombe was appointed Vice-President, Engineering and Operations to provide focused, senior management attention on major projects and energy purchase agreements, and to address heightened concern for environmental issues.

To provide renewed corporate emphasis to Customer Service and further emphasis to the energy management role in the Company, James A. Lea was appointed Vice-President, Customer Service and Energy Management.

Douglas K. McKenney was appointed Vice-President, Finance and Administration to consolidate the support functions of the Company providing administrative service. Mr. McKenney continues as Chief Financial Officer and Corporate Secretary.

Frank McKearney, Supervisor of the Charlottetown Commercial Office is a band enthusiast and Director of Music for the Prince Edward Island Regiment.

In a climate of increasing public involvement in regulatory proceedings, Michael A. Pavey was appointed Vice-President, Corporate Planning to provide assistance in the areas of government affairs and corporate and strategic business development.

Recognizing that our employees are our most valuable resource, we have created the position of Manager, Human Resources, reporting directly to the President.

These changes will allow closer involvement of the senior management team in the direction of the operations of the Company. This will enable the Company to address changes in such issues as government relations, and regulatory and environmental concerns more effectively and provide a heightened awareness of customer service and effective use of our human resources within the Company.

Provincial Regulation

The Company is regulated by the Public Utilities Commission of Prince Edward Island under the provisions of the Electric Power and Telephone Act. This regulation is with respect to rates, capital expenditures, financing and other matters.

This was a busy year in the regulatory field. In January the Public Utilities Commission approved a request by the Company to rebate to our customers excess revenue from 1987, in the amount of $357,000.

The Commission rendered a decision on March 31, 1988 allowing the Company to raise the minimum demand qualifications from 100 to 500 kVA for the Interruptible Rate classification. This allows a more practical level of control for the interruptible portion of our system load.

In November the Public Utilities Commission responded to an application made in anticipation of revenue surplus to revenue requirement. They ordered a rate adjustment causing us to forego revenue during November and December in the amount of $700,000. They further ordered us to return to our customers any remaining surplus after 31 December, 1988. This amounted to $169,000.

As a result of an application by the Company an interim set of rates, tolls, and charges, reflecting a reduction of 1.1 percent in basic rates effective December 1, 1988 to December 31, 1989, was confirmed by the Public Utilities Commission on December 7, 1988. In October 1989 the Company will file further evidence in support of this application.

Amalgamation

In May the Company's Board of Directors voted to amalgamate Maritime Electric Company, Limited and its wholly owned subsidiary, Maritime Electric (PEI) Limited, effective June 30, 1988. The subsidiary was incorporated in 1981 to facilitate the Company's acquisition of our 10 percent ownership in the 200 MW coal-oil fired unit at Dalhousie, NB. In June the Public Utilities Commission approved the amalgamation. To provide for the amalgamation, the Company bondholders approved amendments to the Company's Trust Deed at their June meeting. The Company considers the amalgamation desirable for regulatory purposes, to simplify the Corporate structure and to secure better customer understanding of our operations. The amalgamation will have negligible, if any, impact on the Company's earnings or ability to earn.

Financial Review

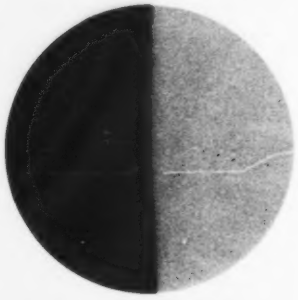
Revenue & Costs

Basic rates, which include a provision to cover the cost of fuel and purchased energy at a 1980 price level, were reduced by 1.1% in December 1988. The cost of fuel and purchased energy was less than the provision for fuel and purchased energy included in the basic rates. Operation of the energy cost adjustment mechanism (fuel clause), which is independent of basic rates and includes a 12 month averaging feature, will refund this over-collection when the price of fuel and purchased energy rises above the base level.

Montague's Merrill Scott fulfills two executive roles, one full-time as Maritime Electric's Eastern District Manager, and the other part-time as Mayor of that lovely town.

Operating revenue in 1988 amounted to $59.9 million, a decrease of 2 percent over 1987 operating revenue.

The disposition of this revenue is shown on the accompanying graph entitled "Revenue and Costs" together with a table showing the 1987, 1988 comparisons.



Revenue and Costs

- 49.3% Cost of generation and purchased energy
- 20.0% Other operating and maintenance
- 8.4% Income Tax
- 7.2% Depreciation
- 7.5% Net Interest and Preferred Dividends
- 4.3% Common Dividends
- 3.3% Earnings re-invested in the Company

Bob Betton is trained to take charge of a tough situation either as a Leading Rural Serviceman based in Sherbrooke, or as an amateur hockey referee.

The breakdown of revenue and costs for the two years is as follows:

$(Millions)	1988	%	1987	%
Sales Revenue	59.9	100	61.1	100
Expenses				
Cost of generation and purchased energy	29.5	49.3	31.7	51.9
Other operating and maintenance	12.0	20.0	11.5	18.8
Income Tax	5.0	8.4	5.4	8.8
Depreciation	4.3	7.2	4.0	6.6
Net Interest and Preferred Dividends	4.5	7.5	4.2	6.9
Common Dividends	2.6	4.3	2.4	3.9
Earnings re-invested in the Company	2.0	3.3	1.9	3.1

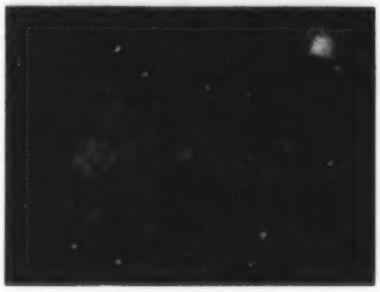
Net Income

Net income increased to $5.3 million from $5.1 million in 1987. These amounts represent the maximum rate of return on common equity allowed by Public Utilities Commission.

Earnings per common share in 1988 amounted to $1.42 compared to $1.34 in 1987. This is based on the average number of common shares outstanding which amounted to 3,174,291 in 1988 compared to 3,140,076 in 1987.

1988 Financing

In June 1988 the Company issued $10 million of First Mortgage Bonds. The issue carries a rate of 11.2 percent and a term of 10 years.



On September 1, 1988 the Company redeemed all its outstanding 14.75 percent $20 par value Series C preferred shares at the redemption price of $21 per share.

During 1988 the Company raised $434,000 of common equity capital through its Consumer and Employee Share Purchase Programs. These Plans have been in effect since 1983.

In the fall of 1988 the Public Utilities Commission of Prince Edward Island approved the change of our Customer Share Purchase Plan to a Consumer Share Purchase Plan. Under the new name the Plan is available to all Island residents whereas previously only Maritime Electric customers were permitted to acquire common stock in the Company during specific times of the year without incurring brokerage fees. The Company's directors have strongly endorsed this initiative to expand our Island shareholder base.

In January 1989 the Company applied to the Public Utilities Commission to allocate a further 70,000 common shares from Treasury toward these Share Purchase Plans. This application was approved on February 22, 1989.

The equity portion of the 1988 capital structure depicted in the accompanying Year-End Capitalization graph combines both preferred and common equity. The graph illustrates the Company's commitment to maintaining a strong equity driven capital structure.

Equity per common share continued to grow in 1988 to $10.65. This growth over the last 5 years is illustrated on page 8.

1989 Financing Requirements

The carryover of a $7.9 million bank loan from December 31, 1988 plus our 1989 Construction Program now estimated at $15.6 million together with cash flow changes, will necessitate 1989 long-term financing in the order of $15 million. Internally generated funds will provide the balance of funding required.

The amendments made in 1988 to the 1955 Trust Deed provide the Company with greater flexibility, particularly in regard to sinking fund requirements for future bond financings.

Accounting for Pension Costs

In January 1989 the Company applied to the Public Utilities Commission for permission to expense for regulatory purposes the amount of Company contributions to the Employee Pension Plan, rather than the amount calculated using the CICA pension expense method. This accounting treatment is expected to result in a more stable means of recovering pension costs through current rates in the regulated environment in which we are operating.

However, 1987 and 1988 pension expense has been calculated using the CICA guidelines in accounting for pension costs.

Impact of Inflation

The cost of the land, buildings, plant and equipment, and associated accumulated depreciation at December 31, 1988 and December 31, 1987 are shown on the basis of both historic and replacement costs. Replacement cost is estimated using various price indices and applying them to the different types of property according to age. Accumulated depreciation on replacement cost has been determined based on the results of a depreciation study.

	1988		1987	
($'000)	Original Cost	Current Cost Basis (Indexed)	Original Cost	Current Cost Basis (Indexed)
Land, Buildings, Plant and Equipment	136,023	296,722	125,595	284,983
Less: Accumulated Depreciation	45,298	136,212	41,737	136,233
Net	90,726	160,510	83,857	148,750

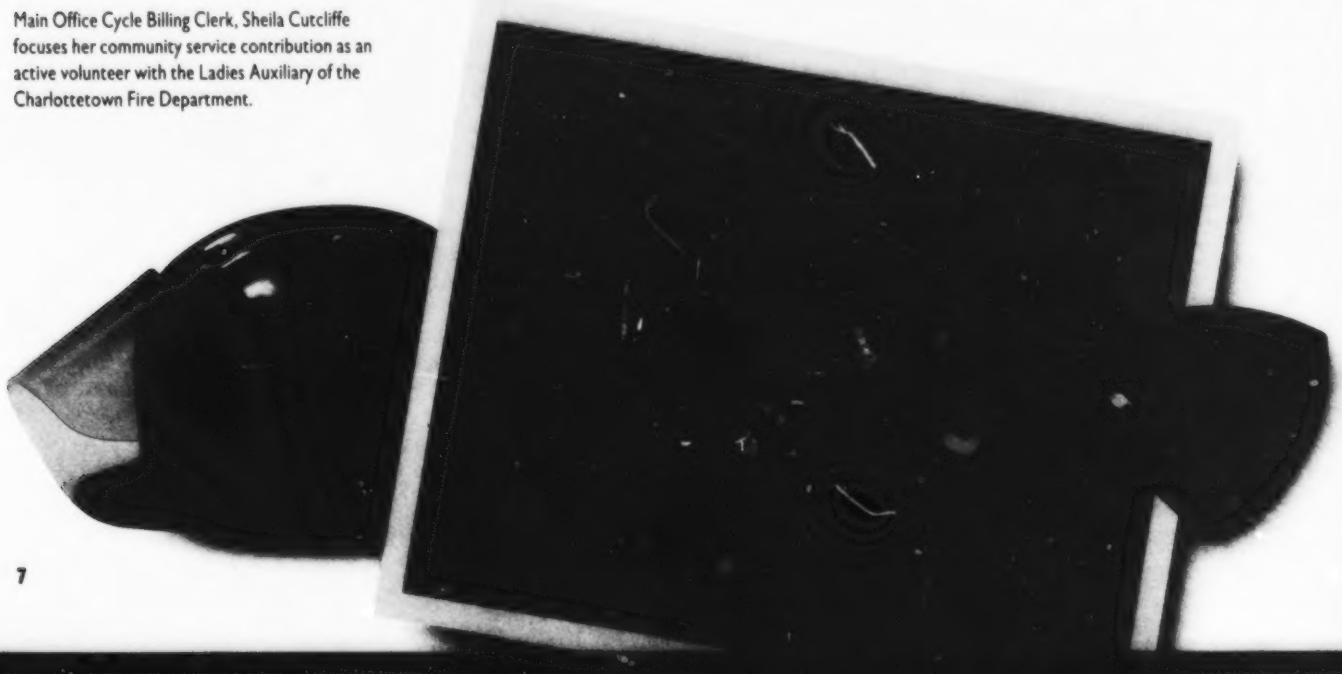
It is with deep regret that your Directors record the death on December 3, 1988 of Mr. Jack Boomhower. Mr. Boomhower was an electrical engineer who joined Maritime Electric in 1953. An officer of the Company since 1971, he held various positions of increasing responsibility. At the time of his death he held the position of Director of Facilities Planning, responsible for the long range physical planning and construction functions in the Company. His knowledge and presence will be missed.

This report together with the financial statements for 1988 are submitted on behalf of the Board of Directors.

R.W. Smith
Chairman of the Board

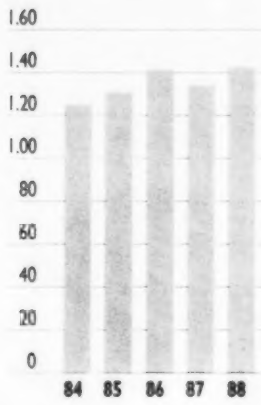
J.H. Reynolds
President and Chief Executive Officer

Main Office Cycle Billing Clerk, Sheila Cutcliffe focuses her community service contribution as an active volunteer with the Ladies Auxiliary of the Charlottetown Fire Department.



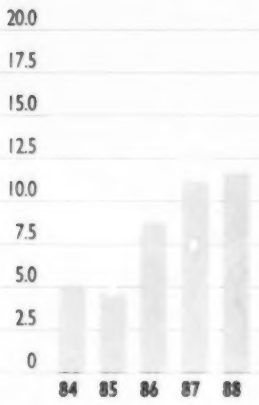
FINANCIAL YEAR AT A GLANCE

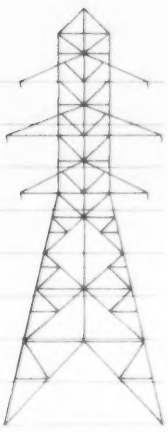
Earnings per Share
(in dollars)



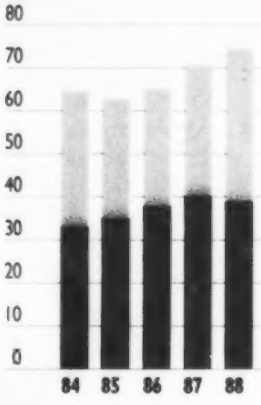
Equity per Share
(in dollars)

Capital Expenditures (Net)
(millions of dollars)

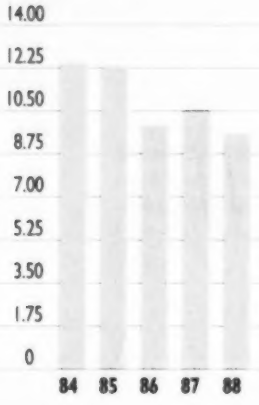




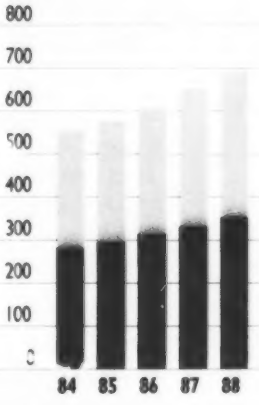
Year-End Capitalization
(millions of dollars)

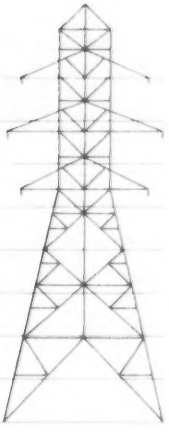


Prices of Electricity
(cents per kilowatt-hour)



Distribution of Electricity
(millions of kilowatt-hours)





■ Equity
Debt

■ Residential
■ System Losses
General Service and Other

Summary Of Accounting Policies

Regulation:
The Company is engaged in the purchase and production of electricity in Prince Edward Island and New Brunswick and its sale in Prince Edward Island and is regulated by the Public Utilities Commission of Prince Edward Island under The Electric Power and Telephone Act.

Fixed assets:
Additions are made to fixed assets and costs are capitalized in accordance with the regulations established by the Public Utilities Commission.

The cost of additions to fixed assets represents the cost of materials, related services, direct labour, interest during construction and other applicable indirect overheads.

Interest during construction is calculated on a monthly basis at a rate equal to the rate of return on earnings base approved by the Public Utilities Commission.

Retirements from fixed assets are made to accumulated depreciation on the basis of original cost plus retirement expenses, less salvage.

Depreciation is provided on a straight-line basis using rates which are estimated to amortize the cost of fixed assets, less salvage value, over their useful lives. These rates are periodically reviewed by the Public Utilities Commission. Depreciation on the cost of contributed assets is charged to the contributions account.

Materials and supplies:
Materials and supplies are valued at average cost.

Contributions:
Contributions towards the cost of construction for service connections and those arising from the purchase of lines from the government are deferred. These amounts are written off over the life of the assets by an annual depreciation charge.

Revenue:
Revenue is recognized on billings rendered monthly to customers on a cyclical basis.

Deferred charges:

Financing costs
Costs relating to the issue of bonds and preferred shares are amortized over the estimated minimum life of the issue and those relating to the issue of common shares are amortized over 20 years.

Generation studies
Expenses related to generation planning carried out from January 1, 1985 to August 31, 1988 are amortized over a five-year period commencing in 1989 in accordance with an order by the Public Utilities Commission.

Engineering studies
Expenses related to engineering studies are deferred until a project is approved by the Public Utilities Commission at which time the expenses are capitalized in fixed assets. If the studies do not lead to an approved project, the expenses are charged to operations.

Deferred energy cost adjustment:
The Company's rates include an energy cost adjustment factor representing the difference between actual fuel costs and an approved base fuel cost which is recoverable from or refundable to customers based on a moving average formula. Amounts not refunded or recovered at December 31 are deferred.

Management's Report

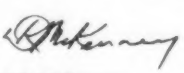
The accompanying financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada using procedures established by management and the framework of accounting policies outlined above. In management's opinion they fairly reflect, within reasonable limits of materiality, the Company's financial position, results of operations, and changes in financial position for the fiscal period ended December 31, 1988. Financial and other operating data contained elsewhere in this report are consistent with the financial statements.

Responsibility for the financial statements to shareholders rests with the Board of Directors.

An Audit Committee of Directors is appointed by the Board to review the financial statements in detail with management and the external auditors, and to report to the Directors prior to their approval of the financial statements for publication.

The Company's external auditors, Price Waterhouse, are appointed by the shareholders to provide an independent review of management's discharge of their responsibilities as they relate to the financial statements prepared by management. The auditors' report is set out on page 12.

J.H. Reynolds
President and Chief Executive Officer



D.K. McKenney
Vice-President, Finance and Administration

BALANCE SHEET

	December 31	
	1988	1987
Assets		
Fixed assets (Note 2):		
Land, buildings, plant and equipment	$136,023,249	$125,594,574
Less: Accumulated depreciation	45,297,734	41,737,106
	90,725,515	83,857,468
Current assets:		
Accounts receivable	4,691,967	5,072,603
Income taxes recoverable	3,831	—
Materials and supplies, at cost	3,514,462	3,306,804
Prepaid expenses	147,530	198,777
	8,357,790	8,578,184
Deferred charges (Note 3):	1,249,810	585,862
	$100,333,115	$ 93,021,514
Shareholders' Equity and Liabilities		
Shareholders' equity (Note 4):		
Common shares	$ 5,011,474	$ 4,577,650
Retained earnings	28,998,710	27,171,998
	34,010,184	31,749,648
Preferred shares	5,400,000	8,500,000
	39,410,184	40,249,648
Long-term debt (Note 5):	27,293,000	17,565,000
Current liabilities:		
Bank indebtedness	7,898,158	13,097,388
Accounts payable and accrued liabilities	5,581,120	6,342,004
Cost-savings refundable to customers	481,725	670,086
Dividends payable	795,698	827,954
Deferred energy cost adjustment	3,862,861	717,517
Income taxes payable	—	195,953
Long-term debt due within one year	185,000	185,000
	18,804,562	22,035,902
Deferred credits:		
Deferred income taxes	7,806,467	7,291,978
Contributions	7,018,902	5,878,986
	14,825,369	13,170,964
	$100,333,115	$ 93,021,514

See accompanying summary of accounting policies and notes.

Approved by the Board:

Director

Director

Statement Of Earnings

	Year ended December 31	
	1988	1987
Operating revenue	$59,866,283	$61,111,248
Operating expenses	41,518,144	43,209,523
Provision for depreciation	4,312,256	4,040,557
	45,830,400	47,250,080
Operating income	14,035,883	13,861,168
Other expenses:		
Interest expense on long-term debt	2,804,860	3,528,489
Interest revenue	—	(174,832)
Other	977,074	(56,504)
	3,781,934	3,297,153
Earnings before income taxes	10,253,949	10,564,015
Provision for income taxes:		
Current	4,464,691	4,699,313
Deferred	514,489	743,450
	4,979,180	5,442,763
Net earnings	5,274,769	5,121,252
Preferred dividend requirements	753,781	911,781
Earnings applicable to common shares	$ 4,520,988	$ 4,209,471
Earnings per common share	$1.42	$1.34

See accompanying summary of accounting policies and notes.

Statement Of Retained Earnings

	Year ended December 31	
	1988	1987
Balance at beginning of year	$27,171,998	$25,386,142
Net earnings	5,274,769	5,121,252
Premium on redemption of preferred shares	(150,000)	—
	32,296,767	30,507,394
Dividends:		
Preferred shares—		
5%	30,000	30,000
Series A	86,625	97,125
Series B	342,156	342,156
Series C	295,000	442,500
Common shares	2,544,276	2,423,615
	3,298,057	3,335,396
Balance at end of year	$28,998,710	$27,171,998

See accompanying summary of accounting policies and notes.

STATEMENT OF CHANGES IN FINANCIAL POSITION

	Year ended December 31	
	1988	1987
Cash from operations:		
Net earnings	$ 5,274,769	$ 5,121,252
Charges to operations of depreciation, deferred income taxes and other items not involving an outlay of cash in current year	4,869,840	4,883,968
Changes in operating working capital:		
Increase (decrease) in payables	2,000,146	(3,419,489)
Decrease (increase) in receivables and materials and supplies	220,394	(1,866,520)
Other	(635,478)	(444,441)
	11,729,671	4,274,770
Less: Dividends paid	(3,330,313)	3,300,563
	8,399,358	974,207
Cash used in capital transactions:		
Expenditures for fixed assets (net)	11,600,127	11,237,712
Redemption of long-term debt	272,000	9,390,000
Redemption of preferred shares	3,250,000	100,000
Purchases of common shares	713	71,727
Debt issue expenses	71,565	—
	15,194,405	20,799,439
Less:		
Issue of long-term debt	10,000,000	—
Contributions for extensions	1,559,740	570,689
Subscription for common shares	434,537	556,491
	3,200,128	19,672,259
	$ 5,199,230	$(18,698,052)
Decrease (increase) in bank indebtedness	$ 5,199,230	$(13,097,388)
Decrease in cash and term deposits	—	(5,600,664)
	$ 5,199,230	$(18,698,052)

See accompanying summary of accounting policies and notes.

AUDITORS' REPORT

To the Shareholders of Maritime Electric Company, Limited:

We have examined the balance sheet of Maritime Electric Company, Limited as at December 31, 1988 and the statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the Company as at December 31, 1988 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Price Waterhouse
Chartered Accountants

Montreal, Quebec, — February 10, 1989

1. Amalgamation:
The Company and its wholly-owned subsidiary, Maritime Electric (PEI) Limited, were amalgamated on June 30, 1988. The 1987 comparative amounts are presented on a consolidated basis.

2. Fixed assets:

	December 31	
	1988	1987
Generating plants	**$ 43,887,307**	$ 42,411,671
Distribution systems	**64,706,058**	57,237,559
Transmission lines and substations	**22,656,002**	22,608,775
Other	**3,552,820**	2,842,420
Property under construction	**1,221,062**	494,149
	136,023,249	125,594,574
Accumulated depreciation	**45,297,734**	41,737,106
	$ 90,725,515	$ 83,857,468

Interest in the amount of $159,000 (1987 — $505,000) has been capitalized during construction.

3. Deferred charges:

	December 31	
	1988	1987
Financing costs	**$ 169,891**	$141,421
Generation studies	**452,214**	—
Engineering studies	**424,912**	132,041
Deferred pension expense	**202,793**	312,400
	$1,249,810	$585,862

4. Shareholders' equity:

(1) Authorized capital —
The authorized capital consists of:
(a) An unlimited number of common shares with no par value.
(b) An unlimited number of cumulative, redeemable, voting preferred shares, issuable in series with the quantities, rights, restrictions and conditions established by the Board of Directors at time of issue.
(c) 6,000, 5%, cumulative, non-voting preferred shares, redeemable at $100 per share.
(d) An unlimited number of 6%, non-cumulative, non-voting preferred shares subordinate to all other preferred shares and redeemable at $10 per share.

(2) Issued capital —

	December 31		December 31	
	1988	1987	**1988**	1987
	(shares)		(amount)	
Common shares (Note 4 (4) (a))	**3,194,483**	3,158,216	**$5,011,474**	$4,577,650
Voting preferred —				
Series A	**40,000**	45,000	**$ 800,000**	$ 900,000
Series B	**40,000**	40,000	**4,000,000**	4,000,000
Series C (redeemed during 1988)	**—**	150,000	**—**	3,000,000
5% non-voting preferred	**6,000**	6,000	**600,000**	600,000
	86,000	241,000	**$5,400,000**	$8,500,000

(3) Voting preferred shares series rights —
(a) Series A shares are entitled to a 10 1/2% dividend and are redeemable after January 31, 1984 at a premium of 6% which reduces to zero by 1992. In addition, five thousand shares are to be redeemed at par each year to meet sinking fund requirements.
(b) Series B shares are entitled to a dividend equal to 52% of the average interest rate on specified five-year guaranteed investment certificates plus 3.25 percentage points. This dividend rate, currently 8.554% (8.554% in 1987), is adjusted at five-year intervals. Commencing in 1987, the shareholders can require an annual redemption of up to 5% of the original issue at subscription value. In 1991 and every five years thereafter, either the Company or the shareholders may require redemption, in whole or in part, of the balance of the issue at subscription value.

(4) Common shares —
(a) Changes in common shares during the year were as follows:

	1988	1987
Shares outstanding at beginning of year	**3,158,216**	3,121,098
Issued under share purchase plans (Note 4(5))	**36,324**	42,454
Purchased for cancellation (Note 4(4)(b))	**(57)**	(5,336)
Shares outstanding at end of year	**3,194,483**	3,158,216

(b) During 1988, the Company purchased for cancellation 57 common shares for $713 cash.

(5) Share option programs —
The Company has a Consumer Share Purchase Plan under which each consumer may make a quarterly subscription for up to $4,000 worth of common shares of the Company at market value and an Employee Share Purchase Plan whereby each employee may subscribe for up to 10% of his pay for the purchase of common shares of the Company at 90% of market value.

Subscriptions of $434,537 (1987 — $556,490) received under these plans resulted in the issue of 36,324 shares during 1988 (1987 — 42,454). A balance of 26,008 shares remains from the original 1983 allotment of 180,000 shares for issuance under these plans.

The Company's Board of Directors has authorized an additional allotment of 40,000 shares under the Consumer Share Purchase Plan and 30,000 shares under the Employee Share Purchase Plan for a total of 70,000 shares. This additional allotment is subject to approval by the Public Utilities Commission.

5. Long-term debt:

		December 31	
		1988	1987
First mortgage sinking fund bonds.			
17-1/4%	due 1990	$ 5,640,000	$ 5,700,000
8-3/4%	due 1993	2,550,000	2,550,000
11%	due 1996	4,000,000	4,000,000
10-3/8%	due 1997	2,800,000	3,000,000
10-3/8%	due 1998	2,488,000	2,500,000
11.2% first mortgage bonds	due 1998	10,000,000	—
		27,478,000	17,750,000
Less: Portion due within one year		185,000	185,000
		$27,293,000	$17,565,000

The first mortgage sinking fund bonds have a sinking fund requirement of 1% of the principal per annum. The annual requirement for sinking fund and for repayment of maturing debt for each of the next five years is: 1989 — $185,000; 1990 — $5,705,000; 1991 — $125,000; 1992 — $125,000; 1993 — $2,525,000.

Pursuant to the terms of the Deed of Trust and Mortgage, the Company has mortgaged or pledged either by way of a first and specific charge or by way of a floating charge all of its properties and assets as security for the first mortgage bonds.

6. Pension costs and obligations:
The Company maintains a contributory defined benefit pension plan covering all of its regular employees. Based on an actuarial report, the present value of accrued pension benefits was $10,369,600 and the value of pension plan assets was $9,208,400.

In 1981 the Company adopted a revised pension plan covering all of its regular employees. All the assets of the previous plan have been absorbed into the 1981 plan.

The Company makes payments to retired employees of supplements to pensions received under the previous plan. Under the 1981 plan it makes payments to retiring employees to bring the pensions payable from the plan assets up to the levels specified under the 1981 plan. Such payments, on the direction of the Public Utilities Commission, are expensed as paid.

TEN-YEAR SUMMARY

Statement of Income ($'000)	1988	1987	1986	1985	1984	1983	1982	1981	1980	1979
Operating Revenue	59,866	61,111	53,994	64,119	61,848	56,965	53,743	45,651	36,261	31,809
Operating Expenses	41,518	43,209	37,037	47,277	45,648	41,360	38,460	35,614	27,512	24,182
Depreciation	4,312	4,041	3,596	3,448	3,310	2,979	2,832	2,256	1,998	1,789
Finance Charges	3,782	3,297	3,171	3,900	3,963	4,104	4,915	2,752	1,943	1,552
Provision for Income Taxes	4,979	5,443	4,875	4,460	4,092	3,990	3,608	2,474	2,267	1,942
Net Earnings	5,275	5,121	5,315	5,034	4,835	4,532	3,928	2,555	2,541	2,605(a)
Balance Sheet Data ($'000)										
Fixed Assets	136,023	125,595	115,751	107,958	103,923	99,473	95,453	83,268	70,140	64,830
Accumulated Depreciation	45,298	41,737	38,735	35,857	32,651	29,723	27,000	24,199	22,131	20,316
Capitalization:										
Total Debt	35,376	30,847	27,140	27,493	31,315	31,531	32,642	30,981	23,829	21,880
Shareholders' Equity										
Preferred	5,400	8,500	8,600	8,700	8,800	8,900	9,000	6,100	2,200	2,300
Common	34,010	31,750	29,479	27,058	24,566	22,814	21,053	17,750	16,954	15,675
Share Data (f)										
Earnings per Common Share ($)	1.42	1.34	1.41	1.31	1.25	1.15	1.16	.77	.87	.89(a)
Dividends per Common Share ($)	.80	.77	.72	.6733	.63	.60	.57	.47	.39	.32
Number of Common Shares										
Outstanding at Year-End (000's)	3,194	3,158	3,121	3,096	3,072	3,042	3,042	2,700	2,700	2,700
Book Value per Common Share ($)	10.65	10.05	9.45	8.74	8.09	7.50	6.92	6.57	6.28	5.81
Market Value per Common Share (b)										
High ($)	13 1/4	14 1/2	14	10 7/8	9 7/8	8 3/4	7	5 1/8	5 3/8	5 1/8
Low ($)	11 1/2	10 1/4	10 1/4	9 5/8	7 5/8	6 5/8	4 1/4	4 3/8	3 7/8	3 5/8
Market Volume —										
Shares Traded (c)(000's)	254.5	276.2	348.7	440.1	179.1	176.7	302.1	112.2	446.7	228.3
Financial Ratios										
Capital Structure (percent)										
Total Debt	47	43	42	43	48	50	52	57	55	55
Preferred	7	12	13	14	14	14	14	11	5	6
Common	46	45	45	43	38	36	34	32	40	39
Coverage (times)										
Total Debt Interest	3.6	3.8	3.6	3.3	3.2	3.0	2.5	2.7	3.2	3.4
Total Debt Interest and Preferred Dividends	2.6	2.6	2.4	2.2	2.2	2.1	2.0	2.0	2.7	2.8
Return on Average Common Equity (percent)	13.75	13.75	15.5	15.5	16.0	16.0	16.4	12.1	14.3	16.1
Regulatory Data										
Return on Average Common Equity (percent) (g)	13.75	13.75	15.5	15.5	16.0	16.0	16.5	16.5	15.0	15.0
Rate Base ($'000)	79,455(e)	56,531(d)(e)	50,524(d)(e)	53,698(d)(e)	55,015(d)	51,491(d)	49,942(d)	49,711(d)	47,204	40,147
Return on Rate Base (percent)										
Allowed	11.34	10.35(d)	11.13-11.30(d)	11.13-10.30(d)	11.60-11.75(d)	11.60-11.75(d)	10.75-12.25(d)	10.75-12.25(d)	9.25-10.0	9.25-10.0
Earned	11.35	10.46(d)	11.29(d)	11.23(d)	10.49(d)	10.7(d)	11.59(d)	9.34(d)	9.49	9.70
Operating Data										
Sources of Energy (million kWh)										
Purchased	472.8	483.0	456.6	433.5	413.2	385.6	392.9	467.8	388.9	361.3
Company Owned Generation	223.4	169.9	151.0	145.5	147.0	145.2	117.6	46.6	125.7	151.0
Total	696.2	652.9	607.6	579.0	560.2	530.8	510.5	514.4	514.6	512.3
Sales (million kWh)										
Residential	274.0	259.2	243.0	230.1	222.1	212.4	200.3	204.8	202.4	198.4
General Service & Other	344.7	320.6	295.6	285.0	271.7	258.0	253.2	255.9	257.4	257.8
Total	618.7	579.8	538.6	515.1	493.8	470.4	453.5	460.7	459.8	456.2
Customers (000's)										
Residential	40.2	39.4	38.5	37.7	36.8	36.0	34.9	34.3	34.3	33.6
General Service & Other	8.4	8.1	7.7	7.4	7.3	7.1	7.4	7.7	7.8	7.5
Total	48.6	47.5	46.2	45.1	44.1	43.1	42.3	42.0	42.1	41.1
Number of Employees	221	202	203	201	195	193	196	196	200	204

Notes:
(a) Includes extraordinary item of $261,160 — gain on sale of office building
(b) Price quoted on the Toronto Stock Exchange
(c) Combined volume of shares traded on the Toronto and Montreal Stock Exchanges
(d) Maritime Electric, Unconsolidated 1981 to 1987
(e) Average 1985-1988 (Year-End 1979-1984)
(f) Share data reflects 3 for 1 Split (June 5, 1986)
(g) Return allowed is imputed

CORPORATE DIRECTORY

Board of Directors

A.D. Cameron
Senior Consultant,
Monenco Consultants
Limited, Montreal, PQ

K.V. Cox
Chairman of the Board,
Bruncor Inc.,
Saint John, NB

B.L. de la Giroday*
Treasury Analyst,
B.C. Hydro, Vancouver, BC

A.S. Gordon*
Consultant, Merrill Lynch
Canada Inc., Montreal, PQ

A.H. Holman, O.C.
Retired,
Charlottetown, PEI

A.W. Howard
Consultant,
Calgary, ALTA.

W.G. Lea, Q.C.
Partner, Campbell, Lea,
Michael, McConnell &
Pigot, Charlottetown, PEI

G.A. McMurdo*
Farmer,
Kensington, PEI

M.A. Pavey
Consultant,
Beaconsfield, PQ

J.H. Reynolds
President and Chief
Executive Officer,
Maritime Electric
Company, Limited,
Charlottetown, PEI

D.A. Scales
President, Island
Fertilizers Ltd.,
Charlottetown, PEI

R.W. Smith
Chairman of the Board,
Maritime Electric
Company, Limited,
Charlottetown, PEI

*Members of the
Audit Committee

Officers

R.W. Smith
Chairman of the Board

J.H. Reynolds
President and Chief
Executive Officer

J.A. Lea
Vice-President,
Customer Service and
Energy Management

D.K. McKenney
Vice-President,
Finance and Administration
& Secretary-Treasurer

P.H. Newcombe
Vice-President,
Engineering and
Operations

M.A. Pavey,
Vice-President,
Corporate Planning

Head Office

Confederation Court Mall,
134 Kent Street,
Charlottetown, PEI
C1A 7N2
Telephone: (902) 566-1599
Telex: 014-44115
Fax: (902) 566-2692

Act of Incorporation
Canada Business
Corporations Act

Auditors
Price Waterhouse,
Chartered Accountants

Banker
Royal Bank of Canada

Counsel
Campbell, Lea, Michael,
McConnell & Pigot
Charlottetown, PEI
Byers Casgrain, Montreal, PQ

**Exchange Listings —
Common Stock**
Toronto Stock Exchange
Montreal Exchange
Ticker symbol — MEC

**Transfer Agent
and Registrar**
Montreal Trust Company,
Charlottetown, Halifax,
Montreal, Toronto,
Winnipeg

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